

**GENCORP**

## Stock Pitch

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## I. Investment Thesis

**GenCorp's valuable intellectual property, dominant competitive advantages, long term sole source contracts, propulsion monopoly, and valuable real estate make it a compelling investment based on prevailing market pricing.**

Recommendation: Buy

Current Price: \$15.31

Price Target: \$24.00

## CATALYSTS

- Realization of real estate value and development of property
- Transformative acquisition and synergies
- Increased efforts towards investor relations

## RISKS

- Sequester and reduction in revenue from NASA contracts
- Emerging competition (SpaceX)
- Lack of experience in real estate development

## **II. Industry and Company Overview**

Small Arms

Armored  
Vehicles

Aircraft

Tactical Missiles

Autonomous  
Weaponry

1900's

2013

## FUTURE OF US MILITARY

- Since 2000, it has been increasingly clear that the U.S. will be unable to devote ground troops to every combat situation in which we are called to arms
  - Instead, **proxy wars** and **tactical strike support** have been increasingly common methods for the U.S. to protect its interests overseas
- In general, we believe this points to the **continued use of medium to large-size liquid-fueled rockets**
  - Purchases of tactical missiles and missile defense will also likely be relatively immune to spending cuts from the sequester
- While we think it is very hard to predict which companies will successfully develop the best explosive configurations and targeting systems, there is a **distinct investment opportunity in rocket propulsion**

## OVERVIEW

- **GenCorp** is an aerospace company with two divisions:
  - **Aerojet-Rocketdyne**, a supplier of premium rocket propulsion technologies
  - **Easton**, a recently formed group that manages GenCorp's real estate holdings



**Strategic Propulsion**



**Tactical Propulsion**



**Missile Defense Systems**



**Spacecraft Propulsion**

## FINANCIAL OVERVIEW

*(\$ in millions, except per share data)*

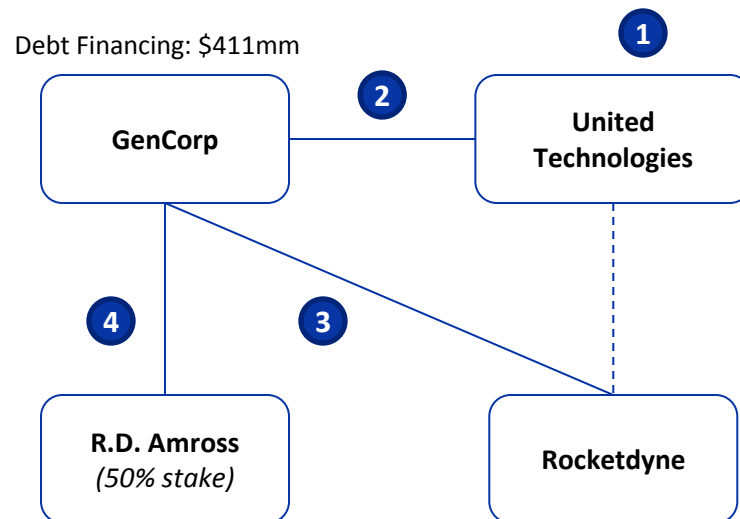
<i>Common Stock (Ticker GY)</i>	\$15.31
Outstanding Equity Instruments	
Common Stock	59.5
Dilutive Shares from Options	0.0
<b>Total</b>	<b>59.5</b>
Equity Value	\$910.9
- Cash and Cash Equivalents	(169.2)
+ Total Debt	704.6
+ Minority Interest	0.0
<b>Enterprise Value</b>	<b>\$1,446.3</b>

	Metric	Multiple
2012A Revenue	\$1,695.0	<b>0.9x</b>
2013E Revenue	1,775.0	<b>0.8x</b>
2012A EBITDA	\$205.6	<b>7.0x</b>
2013E EBITDA	226.0	<b>6.4x</b>

## OVERVIEW

- Rocketdyne was previously owned by United Technologies Corp
  - GenCorp was the only logical strategic buyer
- Creates an effective monopoly on medium and large-sized liquid-fueled rocket engines
  - “The FTC said that it approved the deal even though it would give GenCorp a monopoly in the market for a certain type of high-performance missile defense interceptor propulsion system, because the Defense Department wanted to see the transaction go forward.” -Reuters
- Other Transaction Notes:
  - Acquisition doubles the size of GenCorp
  - Highly accretive at **4.5x 2013 EBITDAP**
  - Creates economies of scale and complimentary product offerings
  - Also adds a significant debt load to the pro forma entity

## ACQUISITION DYNAMICS

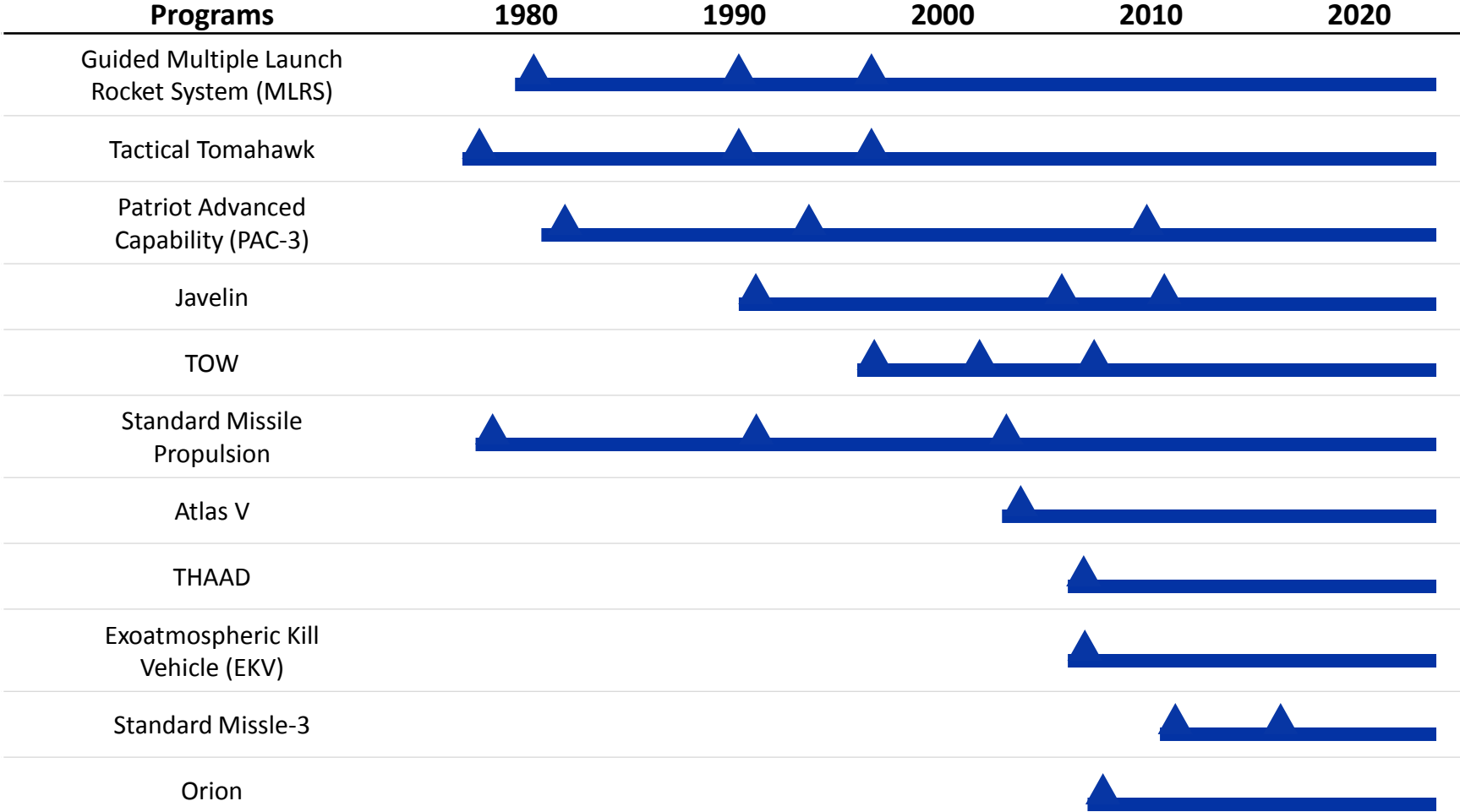


1. United Technologies sells subsidiary Rocketdyne to raise cash for Goodyear acquisition
2. Department of Defense mandates acquisition despite creation of propulsion monopoly
3. GenCorp pays United Technologies Corp. **\$411mm**, which was financed through raising debt
4. An additional **\$55mm** will be paid upon acquisition of UTC's 50% ownership in R.D. Amross (joint venture with a Russian Company)



### **III. Core Businesses**

# Stability of Contract Revenue



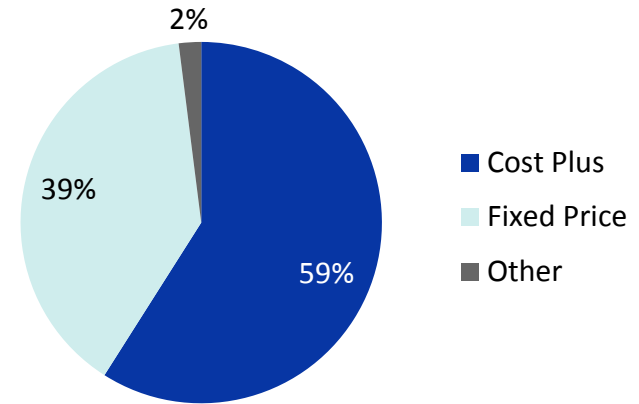
▲ = New Product

# Customer Breakdown

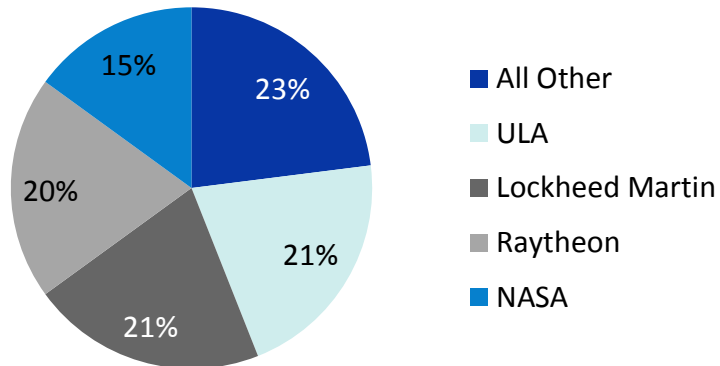
## DOMINANT COMPETITIVE POSITION

- GenCorp's moat In missile propulsion is impenetrable
- GY operates primarily on **sole-source, long-term contracts** (90%)
  - Customer emphasis on risk-avoidance
- Aerojet has served its two largest customers, Raytheon and Lockheed for more than 25 years each
  - Rocketdyne has supplied NASA and ULA for more than 50 years
- Long certification process for new market entrants
- Wide Range of contracts and work despite few customers
  - Literally rocket science

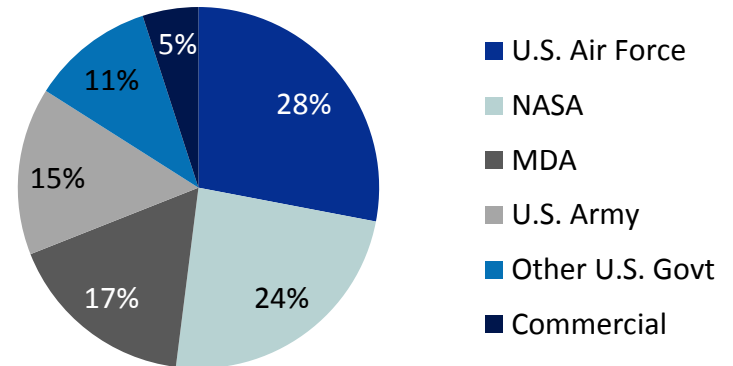
## CONTRACT TYPE



## DIRECT CONTRACTOR



## END USER



# Propulsion Monopoly



Company	Parent	Propulsion Type	Propulsion Application
Aerojet	GenCorp Inc.	<b>Solid, Liquid, Air-Breathing, Electric</b>	Launch, In-Space, Tactical
Alliant Techsystems	Alliant Techsystems	Solid, Air-Breathing	Launch, Tactical, Strategic, Missile Defense
Astrium	European Aeronautics Defense & Space Co.	Solid, Liquid	In-Space
Avio	Avio S.p.A	Solid, Liquid	Launch, In-Space
Electron Technologies	L-3 Communications Corp.	Electric	In-Space
Moog	Moog	Liquid, Electric	In-Space, Missile Defense
Northrop Grumman Space Tech	Northrop Grumman	Liquid	In-Space
Pratt & Whitney Rocketdyne	United Technologies Corp.	<b>Liquid, Air-Breathing, Electric</b>	Launch, In-Space, Missile Defense
Safran	Safran	Liquid	Launch, Tactical
SpaceX	SpaceX	Liquid	Launch, In-Space
Nammo Talley	Nammo Talley	Solid	Tactical

# GAAP & Customer Subsidies



(\$ in millions, except per share data)

## HIGH, STABLE CASH EARNINGS

- Most pension expenses are non-cash and subsidized
  - Aerojet's legacy pension expenses are non-cash until 2015 due to MAP-21
  - Post-2015 pension expenses are heavily subsidized by the gov't due to CAS 412 and CAS 413
    - PV of savings: \$830m (using 7% discount rate)
- R&D Expenses are mostly customer subsidized:
  - GenCorp pays for between 6 and 10% of R&D costs
- High percentage of cost-plus contracts mitigates margin risk and the chance of projects going over budget

YEAR	SALES TO U.S. GOV.	% OF SALES
2010	\$936.9	92%
2011	855.8	93%
2012	786.1	94%

## YEAR

## PENSION EXPENSE

2013	\$131.6
2014	129.3
2015	126.5
2016	123.2
2017	119.8
2018-2022	544.8

## YEAR

## GENCORP R&D

## CUSTOMER R&D

2010	\$17.4	\$283.7
2011	27.4	276.0
2012	30.3	271.8

<http://www.youtube.com/watch?v=jIIR0qW0fnc>

## WARREN BOLEY (CEO)

- Developed **solar electric propulsion technologies** that were already being used to power "some very big" U.S. government satellites that he was not allowed to identify
  - Seeing a huge number of orders from satellite manufacturers
  - Dramatically lowers the cost of launching satellites into orbit by reducing fuel
    - Fuel is often the biggest weight item on a satellite
- Developed a **silent propulsion system**
  - Useful on unmanned planes
- Developed a **hypersonic motor**
  - All three major competitors - Boeing Co (BA.N), Raytheon Co (RTN.N) and Lockheed Martin Corp (LMT.N) – used the motor in rival bids to design a next-generation missile
  - Allows missiles to travel at Mach 4, or four times the speed of sound,
- **The new technology could generate up to \$10 billion in new weapons sales in coming years**

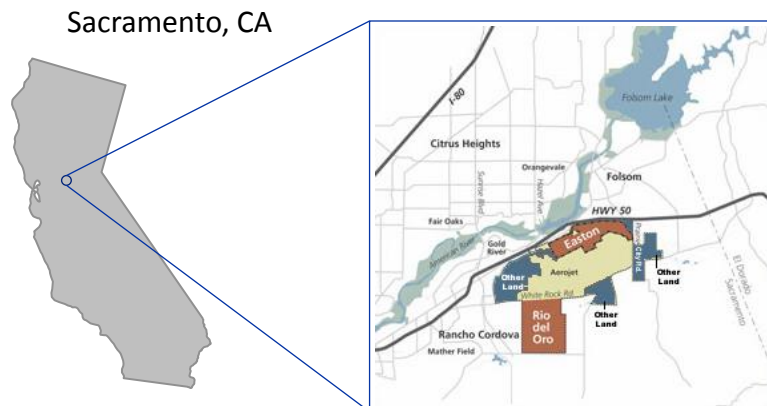
"It's a game changer. It's revolutionary. It's not just 10 percent more," Boley said, adding that he expected the solar propulsion system to generate billions of dollars in orders.

*Warren Boley, CEO of GenCorp <sup>(1)</sup>*

(1): [http://www.sec.gov/Archives/edgar/data/40888/000092189513001268/ex991to8k07319\\_06162013.htm](http://www.sec.gov/Archives/edgar/data/40888/000092189513001268/ex991to8k07319_06162013.htm)

(\$ in millions, except per share data)

## LAND LOCATION



## ESTIMATE OF VALUE

- Based on going rates for commercial and residential real estate in the Sacramento market:
  - Estimated Land Value: **\$400mm-\$1b**
  - Current Enterprise Value: **\$1.45b**

	Bear	Base	Bull
Pretax	\$367	\$611	\$857
Tax	\$116	\$202	\$288
After Tax	\$251	<b>\$410</b>	\$569

## PROPERTY DEVELOPMENT

- GenCorp owns approximately **12,200 acres** of land in the Sacramento metropolitan area
  - 6,000 acres are undergoing entitlement and have been zoned for development
  - Development Agreement completed in 2011 for 1,400 acres; project fully entitled
- Easton expected real estate development:
  - 6,044 acres
  - 18,508 housing units
  - 12.7 million square feet of commercial and retail



## IV. Valuation

# Valuation – Discounted Cash Flow



(\$ in millions, except per share data)

FCF Calculation						
	2014	2015	2016	2017	2018	Terminal Value
Revenue	\$1,850.0	\$1,905.5	\$1,962.7	\$2,021.5	\$2,082.2	
Unlevered FCF Margin	9.5%	9.5%	9.5%	10.3%	10.5%	
Post-Tax Synergies	\$16.3	\$16.3	\$16.3	\$0.0	\$0.0	
Free Cash Flow	192.0	197.3	202.7	208.8	219.2	2,214.0
<b>PV FCF</b>	<b>\$173.0</b>	<b>\$160.1</b>	<b>\$148.2</b>	<b>\$137.5</b>	<b>\$130.1</b>	<b>\$1,313.9</b>

Assumptions	
Prepetual FCF Growth Rate	1.0%
2014-18 Revenue Growth Rate	3.0%
WACC	11.0%

Share Price Calculation	
PV of FCF	\$2,062.8
+ Cash	170.0
-Debt	(504.0)
+ Real Estate	410.0
- Pension Lia	(80.0)
- Environ Lia	(60.0)
<b>Equity Value</b>	<b>\$1,998.8</b>
Diluted Shares Out.	83.3
<b>Share Price</b>	<b>\$24.00</b>

# No Growth Valuation



(\$ in millions, except per share data)

FCF Calculation						
	2014	2015	2016	2017	2018	Terminal Value
Revenue	\$1,850.0	\$1,850.0	\$1,850.0	\$1,850.0	\$1,850.0	
Unlevered FCF Margin	9.5%	9.5%	9.5%	10.4%	10.6%	
Post-Tax Synergies	\$16.3	\$16.3	\$16.3	\$0.0	\$0.0	
Free Cash Flow	192.0	192.0	192.0	192.0	195.7	1,779.1
<b>PV FCF</b>	<b>\$173.0</b>	<b>\$155.8</b>	<b>\$140.4</b>	<b>\$126.5</b>	<b>\$116.1</b>	<b>\$1,055.8</b>

Assumptions	
Prepetual FCF Growth Rate	0.0%
2014-18 Revenue Growth Rate	0.0%
WACC	11.0%

Share Price Calculation	
PV of FCF	\$1,767.6
+ Cash	170.0
-Debt	(504.0)
+ Real Estate	410.0
- Pension Lia	(80.0)
- Environ Lia	(60.0)
<b>Equity Value</b>	<b>\$1,703.6</b>
Diluted Shares Out.	83.3
<b>Share Price</b>	<b>\$20.45</b>